



Memorandum

TO: HONORABLE MAYOR AND
CITY COUNCIL

FROM: Scott P. Johnson

SUBJECT: SEE BELOW

DATE: June 2, 2005

Approved

/s/

Date 06/02/05

**SUBJECT: REPORT ON RESULTS TO COLLECT DELINQUENT ACCOUNTS,
INCLUDING WAYS TO INCREASE COLLECTION EFFORTS**

BACKGROUND

The Mayor's March 16, 2005 Budget Message for Fiscal Year 2005-06 requested that the City Manager report back on the results of the City's strategy to collect on delinquent accounts, including ways to increase collection efforts.

Over the past several years, the Finance Department has strategically re-aligned the Treasury Division's work plan to reduce the level of delinquent accounts Citywide and has increased efforts to conduct fee and tax compliance reviews to assure the City is paid amounts due consistent with the City's Municipal Code and various contractual agreements.

This report describes the City's delinquency management and revenue compliance programs implemented through the Finance Department and provides an overview of collection results experienced from July 2003 through April 2005. This report also includes a section describing and suggesting alternative means by which collection efforts may be further enhanced.

ANALYSIS

The Finance Department's Treasury Division manages the everyday collection and processing of City-wide revenues. In an effort to assure taxes, fees and charges for City services are paid correctly and timely, Treasury proactively engages in various delinquency management and tax/fee compliance programs, resulting in increased revenue and cash flows. These programs were implemented to assure the City receives the maximum benefit to facilitate the delivery of City services provided by specific revenue and cash streams. It should be noted that all of the collection programs are balanced with education, outreach and compliance/enforcement. As collection of revenues due to the City to fund City services is a high priority for the Treasury Division, it is also important that our collection efforts include outreach and education to assure, to the extent possible, that our residents and businesses are aware of the City's requirements in respect to fees, charges for services, and taxes.

It should be mentioned that a report on Finance Department Revenue Collection Efforts was presented to the City's Finance and Infrastructure Committee on June 26, 2002 and subsequently, to the City Council on August 6, 2002. This report outlined the Finance Department's proactive efforts as they relate to revenue collection and delinquency management and demonstrated the "rate of return" experienced as a result of the efforts.

The information provided below is presented similar to that in the June 2002 report, discussing the delinquency management and compliance programs currently in place along with the current "rate of return". As previously mentioned, this information represents the efforts for the period of July 2003 through April 2005. Attachment A summarizes the results for all programs discussed as part of this memorandum.

Delinquency Management Programs

Accounts receivable invoices are generated for a variety of services provided by several different City departments. Ultimately, the Finance Department is responsible for the collection of all monies due the City. To this end, staff periodically evaluates outstanding amounts due, prioritizing for collection of those accounts which are seriously delinquent and/or owe significant amounts for services provided. Follow-up on accounts prioritized for collection is completed by the Treasury Division's Investigator Collectors, who are trained to use an array of collection mechanisms. Typically, individuals with outstanding amounts owed the City are notified by mail of the amount due and called if the account remains outstanding for longer than 90 days. When necessary, payment plan agreements and other means to collect, including obtaining judgments and use of a collection agency, are employed to further collection efforts.

Attachment A provides a summary of revenue derived during the period and related costs yielding a "rate of return" to the City of \$10.19 for each dollar spent in the Finance Department's Delinquency Management Program. Listed below are efforts currently in place to enhance the level of collections in the Finance Department's Delinquency Management Programs.

➤ Seriously Delinquent Accounts Receivable Collections

The delinquency management program as it relates to the collection of outstanding, aged receivables, is very important to the overall revenue collection program due to its cash receipt implications. Proper management of delinquencies increases cash flow for both investment and funds required for payment of City programs. Since the beginning of fiscal year 2003-04, staff has collected more than \$ 2.85 million in Citywide accounts receivable which were 180 days or more outstanding (seriously delinquent) at the time of collection. This strategy, aimed to reduce aging accounts receivable which may otherwise be subject to future write-off, has proven to be very successful.

Comparing the revenue collected through this program since July 2003 of \$2.85 million with staff costs of \$189,403 to collect these delinquencies, this translates into an additional \$15.05 cash collected for each dollar of corresponding cost to collect.

➤ Lien and Assessment Process

Certain citywide programs specifically identified by the San Jose Municipal Code allow the placement of liens and/or assessments on real property once all other efforts to collect amounts owed the City have been exhausted. Staff is currently using the lien/assessment process for the following programs:

- Sidewalk Repairs (Commercial and Rental Properties)	- Recycle Plus Refuse Billing
- Administrative Remedies (Penalties for non-compliance with code requirements)	- Abatements (Cost for actions taken by City to eliminate blight and/or unsafe conditions)

As part of the normal collection process, delinquency notices are sent to property owners receiving services for the above mentioned programs for amounts remaining unpaid for a defined period of time. Amounts due which remain outstanding after proper noticing are subjected to the lien/assessment process.

Staff works closely with the Santa Clara County Recorder's Office and City departments administering these programs to properly notify property owners of amounts due, ultimately leading to the placement of a lien/assessment if the amount remains unpaid. For the period of July 2003 through April 2005, the City has or will collect \$2,157,860 as a result of property owners paying liens or collection through the assessment process, respectively. Compared with staff costs of \$277,571 to administer these programs, this translates into an additional \$7.77 cash collected for each dollar of corresponding cost to collect.

➤ Small Claims Court and Franchise Tax Board Intercept Program

As a means to collect on certain debts owed the City, and as a last resort, staff works with both the City Attorney's Office and the Small Claims Court to obtain judgments for amounts due. Upon receipt of a judgment, staff must work diligently to collect the amount due using all legal remedies. One such legal remedy is the State of California Franchise Tax Board Interagency Intercept Collection Program (Intercept Program).

The Intercept Program allows local agencies to collect delinquent amounts owed by intercepting tax refunds of individuals who owe these amounts. In November 2004, the City began using the Intercept Program, submitting approximately \$363,000 in claims with the State.

To date, the City has received \$19,000 from the Intercept Program and \$27,500 through the City's collection efforts utilizing Small Claims Court. Compared with staff costs of \$25,006 to administer these programs to date, this translates into an additional \$1.86 cash collected for each dollar of corresponding cost to collect. This amount is expected to increase as the Franchise Tax Board processes State tax returns for the current year.

Revenue Compliance Programs

To assure the City receives correct amounts of revenues owed the City for various tax and fee programs, the Finance Department manages a revenue compliance program. Objectives of the revenue compliance program include verifying amounts submitted are correct and consistent with defined requirements in addition to providing education and outreach to entities with respect to proper collection and remittance of revenues.

Staff performing revenue compliance reviews understand the administrative requirements for specific programs and utilize auditing, reconciliation and technical skills to perform the reviews. Additionally, the City employs a revenue consultant to assist staff with certain complex regulatory programs.

Attachment A provides a summary of revenue collected and the related costs for the Finance Department's revenue compliance program which has yielded a "rate of return" of \$2.28 for each dollar spent during the period. Listed below is a description and the results achieved during the period of the revenue compliance programs currently managed by the Finance Department:

➤ Business Information Management System (BIMS) Leads Project

The Business Information Management System (BIMS) compares various third-party independent business lead source data files (e.g. State of California Franchise Tax Board, State Resale Permits, Fictitious Business Filings, etc.) to the City's Business Tax Billing System to identify businesses not in compliance with the business tax ordinance. This project, which began in May 2003, is strategically aimed to provide education and outreach to City businesses while increasing overall compliance. Since the beginning of fiscal year 2003-2004, the BIMS project has yielded business tax, penalty and interest revenue of approximately \$2.5 million. Costs to conduct the BIMS Project over the same period of time total approximately \$1 million (including software fees, supplies, postage and Finance staff costs), translating to \$2.50 of revenue for each dollar of corresponding cost.

It should be mentioned that during the course of conducting the BIMS project, several changes to the City's Business Tax Ordinance were approved by the City Council. Changes made include the addition of business tax exemptions for financial hardship and family caregivers, and increasing the authority of the Director of Finance to review business tax penalties and interest on a case-by-case basis.

➤ Sales Tax Compliance Reviews

The City receives a specified share of the sales tax collected by the State for sales transactions conducted within the City of San Jose. At the present time, the Finance Department manages a contract between the City and MBIA Municipal Services Company (MMC) to help assure the City receives the proper allocation of the sales tax from applicable businesses and the State. MMC is contracted by several municipal jurisdictions throughout the State to assist with sales tax compliance. Services provided to the City by MMC complement the sales tax compliance activities performed by the City Auditor's office.

For the period of July 2003 through April 2005, MMC has derived \$593,230 in additional sales tax revenues at a cost of \$99,343 (consultant contract fees and Finance staff cost). This translates into an additional \$5.97 of revenue for each dollar of corresponding cost.

➤ **Transient Occupancy Tax Compliance Reviews**

A Transient Occupancy Tax (TOT) is levied on each transient guest staying at one of the City's many hotels, motels, and inns. The tax, which is currently set at 10% of the charge for the room only, benefits the City's General Fund (4%) and the City's Transient Occupancy Tax fund (6%). The City has maintained an agreement with TCS Consulting Services for the primary objective to assist the Finance Department with ongoing compliance reviews of the City's transient occupancy tax payers. Each of the City's hotels, motels, and inns has since been reviewed by TCS using a multi-year phased approach. Since contracting with TCS in January 2001, the City has collected \$221,900 to date.

TCS continues to conduct reviews on behalf of the City to assure hotels/motels are in compliance consistent with provisions outlined in the San Jose Municipal Code. In cases in which hotels/motels/inns are not in compliance with the City's Code, follow-up is conducted that typically results in audit findings which generate additional TOT revenue to the City. For the period of July 2003 through April 2005, the Finance Department, working with TCS, has derived \$58,102 in additional TOT due to these reviews, at a cost of \$94,130 (consultant contract fees and Finance staff cost). This translates into an additional \$0.62 derived for each dollar of corresponding cost. However, it should be noted that several compliance reviews are pending resolution with the hotels/motels/inns which will generate additional revenue to the City resulting in a higher return on our investment.

➤ **Utility User Tax Compliance Reviews**

Utility User Taxes (UUT) are imposed on users of electricity, gas, water, and telephone usage. The tax is currently 5% of the amount due for usage of the above referenced services. The City has maintained an agreement with TCS Consulting Services to assist the Finance Department with ongoing compliance reviews of the City's UUT payers. To date, TCS has assisted with the compliance reviews of electricity, gas and land-line phone usage. During the upcoming fiscal year, TCS will be focusing primarily on UUT compliance as it relates to cell phone usage while assisting the City with collection of several outstanding compliance reviews previously completed.

For the period of July 2003 through April 2005, the Finance Department, working with TCS has derived \$429,297 in UUT at a cost of \$323,731 (consultant contract fees and Finance staff cost). This translates into an additional \$1.33 derived for each dollar of corresponding cost.

➤ **Disposal Facility Tax/Solid Waste Enforcement Fee Compliance Reviews**

The City collects Disposal Facility Taxes (DFT) and Solid Waste Enforcement Fees (SWEF) from each of the four primary landfills operated within the City limits. These taxes/fees are levied based on the tonnage of waste brought into the landfills by both commercial and

private haulers. The Treasury Division conducts periodic compliance reviews of each landfill to assure proper calculation and collection of both the DFT and SWEF.

For the period of July 2003 through April 2005, Finance Department staff, working closely with the Department of Environmental Services and the City's Local Enforcement Agency, has derived \$418,133 in DFT and SWEF at a cost of \$237,173. This translates into an additional \$1.76 derived for each dollar of corresponding cost.

➤ **Towing Franchise Compliance Reviews**

The City administers contracts with five towing agencies to provide citywide towing services as required. Payment terms to the City are outlined in each contract. The Finance Department, working closely with the Department of Planning, Building and Code Enforcement, conducts annual compliance reviews of each towing agency.

For the period of July 2003 through April 2005, eleven compliance reviews have yielded \$15,430 in additional revenue at a cost of \$3,270. This translates to an additional \$4.72 derived for each dollar of corresponding cost.

Additional Ways to Increase Collection Efforts

To further enhance revenue and cash collection efforts, consideration should be given to the following alternatives. However, it should be noted that most of the alternatives would require budget resources. Therefore the return on investment and cost benefits should be considered prior to providing direction to implement any of the options listed below:

➤ **Increase Collection Resource Allocation**

Although it is difficult to allocate additional staffing and other related funding for administrative functions in the current budget environment, after considering the potential benefit of assigning additional collection staff to the Finance Department's delinquency management and revenue compliance programs, Council may consider allocating additional resources to further these efforts. Based on the results of the period reviewed per Attachment A, in which the City realized a \$10.19 return for each dollar spent on the delinquency management program and \$2.28 per each dollar spent on the City's revenue compliance programs, for a total average return of \$4.01 per dollar spent, it is likely that the City could recognize additional revenue and/or a reduction in delinquent amounts owed the City by augmenting this program. Augmentation of the City's existing collection staffing resources would enable the Finance Department to broaden the scope of the delinquency management effort by focusing on a larger set of delinquent accounts (i.e. those outstanding for more than 90 days as opposed to 180 days). Expanding this effort would likely result in a higher collection factor, shorten the average number of days that receivables remain outstanding, and fewer accounts becoming uncollectible due to expired collection statutes and/or an inability to find the debtor.

➤ Collaborate with other City Departments on Revenue Compliance

A variety of programs providing services for which charges are levied are managed Citywide. During the period of July 2003 through April 2005, the Finance Department has been proactive in providing these departments with collection and compliance assistance as it relates to program objectives. Recent successful examples of this effort include the compliance reviews conducted for the City's towing contractors and assistance provided to the Fire Department for collection on delinquent permit accounts.

To further the effort of collaborating with other departments, Finance can prepare an inventory of revenue-generating programs managed by other City departments. This program inventory can be used to determine if opportunities exist whereby Finance staff can contribute a value-added component to a program, potentially leading to increased cash and/or revenue generation. A possible candidate for this process might be the parking ticket program currently managed by the Department of Transportation (DOT).

Presently, the City contracts with Turbo Data, Inc. to process all parking citations. Monies paid for parking infractions, less a \$1.95 per-ticket fee charged by Turbo Data, are periodically deposited into the City's account at which time parking ticket revenue is recognized. Parking tickets remaining unpaid, subsequent to the issuance of two delinquency notices by Turbo Data, are turned over to the State of California Department of Motor Vehicles for collection (collections are made when a renewal of vehicle registration is processed). Utilization of this process enables the City to achieve an 80% collection rate for approximately 230,000 parking tickets issued on an annual basis, generating \$7 million. By collaborating with DOT and Turbo Data to review the 20% that is not collected, Finance may be able to propose a solution to potentially increase the collection rate. Another opportunity that has been under discussion with the Department of Transportation is reviewing the possibility of bringing the billing and collection of parking tickets in-house. However, additional analysis and resource requirements, as well as technology needs should be assessed.

➤ Expanded Use of Collection Agencies and Revenue Consultants

The City currently contracts with Professional Recovery Systems (PRS) and CBSJ Financial to provide collection services on delinquent accounts receivable assigned by the Finance Department. Accounts may be assigned to either agency subsequent to the City's inability to collect using an array of collection techniques and/or an agency's success in collecting on a certain type of receivable, including general accounts receivable and municipal water invoices. At times, it is more cost-effective to use an agency than to have staff directly involved in the collection process. PRS charges the City 16.9% of successful collections, while CBSJ charges 35%. During the period of July 2003 through April 2005, PRS and CBSJ Financial have collected more than \$35,000 (before fees) in outstanding receivables due the City.

The Finance Department has been contacted by other collection agencies which have indicated a desire to work with the City. As a means to diversify the pool of collection

agencies and potentially take advantage of technological updates and new collection methodologies to increase the collection of delinquent receivables, staff plans to issue a Request for Qualifications (RFQ) during fiscal year 2005-06.

➤ Consolidation Opportunities at the New City Hall

As part of planning the transition to the New City Hall and to assure a high level of customer service is provided once the transition occurs, the Finance Department has been reviewing an array of services provided to City customers. This review is being conducted to determine the impact of collaborating with citywide departments to achieve cost-saving and streamlining efficiencies. A recent success of this effort is the consolidation of Recycle Plus cashiering services within the Treasury Division cashiering area at the current City Hall.

Finance is currently reviewing consolidation of additional cashiering and billing programs once the move to the New City Hall occurs. Staff is working with the Departments of Planning, Building and Code Enforcement, Transportation and Parks, Recreation and Neighborhood Services to consolidate cashiering services provided for various City programs. Additionally, staff is working with the Fire Department to consolidate the Fire Inspection Billing Program into the Treasury Division, where similar billing programs are managed. Assuming the Mayor and Council direct staff to move forward with these efforts, staff expects that these collection efforts will result in both program operational efficiencies and increased collection on delinquent accounts.

➤ Amnesty Program – One Time Revenue Opportunities

To encourage City customers who are delinquent in paying the City's business tax, the Finance Department has proposed a Business Tax Amnesty Program. The Business Tax Amnesty Program provides delinquent taxpayers an opportunity to forgo paying delinquent penalties and interest during a defined amnesty period while becoming compliant with tax requirements. Increased compliance due to the proposed Amnesty Program is anticipated to lead to the collection of an estimated \$1 million in one-time additional business tax revenue. Since the BIMS project previously noted continues to be successful in yielding considerable revenue to the City and thousands of leads remain to be worked, staff plans to defer the business tax amnesty program to late 2005/06.

As a means to decrease the level of outstanding accounts receivable while increasing reviews, it may be advantageous to consider expanding the Amnesty Program to include additional programs for which the City invoices its customers. Potential programs for inclusion as part of the amnesty process are the Administrative Citation program and the City's General Accounts Receivable, which includes billings for administrative remedies, abatements and sidewalk repairs, among others. By expanding the amnesty program to these receivables, the City should be able to yield additional one-time funds that otherwise may be uncollected due to the age of the receivables. In addition, typically customers are more willing to pay debts outstanding during an amnesty period when the amount of debt is reduced by interest and penalties that would otherwise be assessed. If the program was to be expanded, it is important that sufficient staff and non-personal expenditures be allocated to implement the program.

➤ Technology Efficiency Opportunities

The City uses various technology systems and/or database platforms to perform billing and accounts receivable activities for services provided to customers. Many times, customers who are billed for services within one system (i.e. business tax) are also billed for other services using an alternative system (i.e. Fire permits).

Recently, Council approved the implementation of the CUSP Utility Billing System. This system will consolidate data from multiple sources (systems) into one system for customer service efficiency and billing presentation. The City should continue to review the possibility of combining other City billing systems to achieve similar results.

As a means to assure a high rate of collection is achieved using the existing billing systems, staff has conducted parallel database reconciliations to assure correctness in billing for City services. Recent successes in this area include reconciling the Storm Sewer billing database with the City Geographic Information System (GIS). This reconciliation identified developed parcels which were not being billed for storm sewer services, leading to an additional \$75,000 in annual revenue. Additionally, by comparing the customer data residing in the Fire Permit database with that in the Business Tax database, an additional \$14,000 in business tax was collected. Absent the City using a single billing system for all services provided, database reconciliations of this type, resulting in a higher level of billed revenue, should continue.

CONCLUSION

The Finance Department's Treasury Division is responsible for the everyday collection and process of various Citywide revenue streams as noted above. There are several strategic programs currently being utilized to both increase collections of amounts due the City and increase overall revenues. During the period of July 2003 through April 2005, delinquency management programs in place have increased the City's cash flow by \$5,011,860 at a cost of \$491,980, resulting in an additional \$10.19 available for investment and/or expenditures for each dollar of cost. Additionally, revenue compliance programs managed by Finance over the same period of time have generated an additional \$4,009,990 at a cost of \$1,757,647, translating into an additional \$2.28 for each dollar of staff/consultant cost.

The Finance Department will continue to manage existing revenue compliance review programs and continue to explore additional opportunities to implement programs for other taxes and fees collected Citywide. Finance will also continue to seek other ways to decrease the outstanding delinquent receivables to achieve a more consistent and increased cash flow.

/s/

SCOTT P. JOHNSON
Director, Finance Department

ATTACHMENT A

Finance Department Delinquency Management and Compliance Review Efforts

PROGRAM	JULY 2003 – APRIL 2005		
	Additional Revenue / Cash Flow	Staff / Consultant Cost	\$ Generated / Total Cost
Seriously Delinquent Accounts Receivable Collections	\$2,850,000	\$189,403	\$15.05
Lien / Assessment Collection Processes	\$2,157,860	\$277,571	\$7.77
Small Claims Court and Franchise Tax Board Intercept Program	\$4,000 (1)	\$25,006	\$0.16
Total – Delinquency Management Programs:	\$5,011,860	\$491,980	\$10.19
Business Tax Lead Identification (BIMS)	\$2,500,000	\$1,000,000	\$2.50
Sales Tax Compliance Reviews	\$593,230	\$99,343	\$5.97
Transient Occupancy Tax Compliance Reviews	\$53,900	\$94,130	\$0.57
Utility User Tax Compliance Reviews	\$429,297	\$323,731	\$1.33
Disposal Facility Tax / Solid Waste Enforcement Fee Compliance Reviews	\$418,133	\$237,173	\$1.76
Towing Franchise Compliance Reviews	\$15,430	\$3,270	\$4.72
Total – Revenue Compliance Programs:	\$4,009,990	\$1,757,647	\$2.28
TOTAL:	\$9,021,850	\$2,249,627	\$4.01

- (1) The Franchise Tax Board Intercept Program was implemented in March 2005. Staff anticipates amounts collected under the auspices of this program will rise due to the processing of income tax returns submitted to the State by the initial deadline date of April 15, 2005 (\$363,000 in claims submitted to State to-date).